

November 10, 2003

Erie County Legislature
25 Delaware Avenue
Buffalo, New York 14202

Honorable Joel A. Giambra
Erie County Executive
95 Franklin Street
Buffalo, New York 14202

RE: County of Erie 2004 Tentative Budget

Dear Honorable Members and County Executive Giambra:

As the County's Chief Fiscal, Accounting, and Reporting Officer, this Office annually reviews the Tentative Budget and provides comments and observations to you. The purpose of this review is to provide data for you to consider prior to final adoption of the County budget.

Since the 2004 Tentative Budget was released only last week, the documents have not been reviewed in great detail. Despite the time constraints, the following observations are offered for your consideration.

The 2004 Tentative Budget:

- I. Includes \$38,612,462 in budgeted salary savings.
- II. Consumes \$35,000,000 of fund balances in the General Fund, a smaller amount than for each of the past three budgets.
- III. Allocates significant amounts of revenues from the Tobacco Asset Securitization transaction for capital projects (\$17,840,211) and for debt service costs (\$17,885,339).
- IV. Includes local share funding for Social Service Programs of \$235,059,137, an increase of \$30,949,400 over the actual costs for the 12 months ended September 30, 2003.
- V. Continues the policy initiated in 2003 of securitizing property tax liens and includes revenue of \$15,495,000 from this source.

- VI. Presents a capital budget that for the fourth consecutive year is substantially higher than in years prior to 2001 (\$63,021,040).

Following are more detailed commentaries on the 2004 Tentative Budget.

I. BUDGETED SALARY SAVINGS

Page 92 of the Budget Message, attached as Exhibit A, presents a summary of the gross and net costs for 2004 budgeted positions. Budgeted salary savings in the amount of \$38,612,462 are shown under the column heading "Less 2004 Budgeted salary savings."

Attached as Exhibit B is a more detailed schedule, showing the three major components of the total savings:

Savings from budgeted turnover	\$14,963,962
Savings from retirement	17,248,329
Savings from re-engineering initiatives	<u>6,400,171</u>
Total Savings	<u>\$38,612,462</u>

Attached as Exhibit C is an analysis of projected savings from budgeted turnover for the General, Utilities, Road, and Social Service funds. This analysis shows that if the October 17, 2003 employment level is held constant, actual costs will exceed budget by \$0.5 million, or 13 positions.

Attached as Exhibit D is an analysis of estimated savings from employee retirements for the General Fund. Many factors must be considered in order to accurately measure the impact of retirements. Among them are:

- the date the employee is removed from the county payroll,
- the amount of lump sum payouts associated with vacation banks,
- whether or not the employee worked in a position for which salary costs are wholly or partially reimbursed by the state or federal government,
- whether or not the position will be refilled, and when.

Details regarding these factors were not available for our review. Alternatively, in order to provide some insights as to the significance of this budgeted offset to estimated personal service costs, Exhibit D presents different illustrations with variable assumed retirement dates of January 1, April 1, July 1, and October 1. The exhibit shows the number of actual retirements that would be necessary in each illustration in order to yield the budgeted amount of savings for the General Fund. The number of required retirements in 2004 under these illustrations are: 397 if all retire on January 1; 530 if all retire on April 1; 795 if all retire on July 1; and 1,589 if all retire on October 1. The second illustration shows the variable amount of savings to be achieved if there are 397 retirements at four different times of the year.

Attached as Exhibit E is an analysis of savings from the re-engineering initiative. Details of the re-engineering savings were not available for our review. Alternatively, Exhibit E presents

illustrations with the same variable termination dates used for retirement savings. The number of required 2004 terminations are: 147 if all were effective January 1; 197 if all were effective April 1; 295 if all were effective July 1; and 590 if all were effective October 1.

The total \$38,612,462 in projected savings from normal turnover, retirements, and re-engineering represents a bold and aggressive initiative by the Administration. It is imperative that the level of filled positions be monitored closely throughout 2004.

II. USE OF FUND BALANCE

Within the \$911.5 million total 2004 Tentative Budget, the General Fund (General and Social Services funds combined) accounts for approximately \$785.2 million. The amount of fund balance being used to balance the General Fund budget is \$35 million. The specific sources of General Fund fund balance to finance appropriations in 2004 are:

Item 1. "Appropriated Fund Balance," Book A, Page 199 Representing the two-year rule or Unreserved, Undesignated General Fund fund balance from the audited 2002 financial statements. The Erie County Charter mandates that it be used in the 2004 Budget.	\$20,553,673
Item 2. "Appropriated Fund Balance-ECMC," Book A, Page 199 Representing a portion of the \$24.8 million Designated for ECMC in the audited 2002 financial statements.	<u>14,446,327</u>
Total General Fund fund balance used in the 2004 Tentative Budget	<u>\$35,000,000</u>

I have regularly criticized balancing annual budgets with significant amounts of windfalls and prior year reserves and/or designations. Rather than relying on reserves and/or designations, recurring expenditures should be financed from recurring revenue. The following schedule presents the amount of fund balance and other non-recurring resources used to balance the General and Debt Service Funds since 1989.

(Amounts shown in thousands)			
<u>Budget Year</u>	Two-year Rule	Current Year Variance & Other	<u>Total</u>
	<u>Undesignated Fund Balance</u>	<u>Prior Year Resources</u>	
1989	\$ 3,805	\$ 2,089	\$ 5,894
1990	294	3,367	3,661
1991	2,341	8,137	10,478
1992	3,771	15,168	18,939
1993	267	11,217	11,484
1994	3,001	21,281	24,282
1995	973	16,392	17,365
1996	2,868	38,911	41,779
1997	4,592	23,681	28,273
1998	6,665	34,105	40,770
1999	7,604	58,001	65,605
2000	5,882	46,347	52,229
2001	14,961	63,073	78,034
2002	6,813	57,656	64,469
2003	26,166	29,638	55,804
2004	20,554	17,443	37,997

On a positive note, there is a reduction in the amount of fund balance being used in the 2004 budget. It is also significant that, per the Budget Message (Page 7), the Administration has pledged to avoid the need to use unreserved fund balance in 2005 by aggressively pursuing various re-engineering strategies and other cost-containment initiatives.

III. TOBACCO SECURITIZATION PROCEEDS

The 2004 Tentative Budget relies heavily on the use of tobacco securitization proceeds not only for capital project purposes, but also for debt service, as follows:

2004 TENTATIVE BUDGET USE OF TOBACCO REVENUES

General Debt Service, Book C, Page 147	\$14,028,681
ECMC Healthcare Network Debt Service	<u>3,856,658</u>
Subtotal – tobacco monies used for debt service	17,885,339
Capital Projects (excluding ECMC Healthcare Network)	6,188,540
Capital Projects-ECMC Healthcare Network, Book A, Page 199)	<u>11,651,671</u>
Total tobacco securitization proceeds proposed for use	<u>\$35,725,550</u>

The \$35,725,550 budgeted in 2004 represents a decrease of \$1,105,360 from the amount included in the 2003 budget.

With the budgets for the Debt Service Fund and the ECMC Healthcare Network each benefiting from the receipt of tobacco revenues directly from the Capital Fund, the traditional General Fund subsidies to those funds for debt service can be reduced by a like amount. This means that for 2004, the General Fund saves \$17.9 million as a result of the Administration's 2002 plan to use tobacco money for debt service for the years 2002 through 2006.

IV. SOCIAL SERVICES PROGRAMS

The 2004 Tentative Budget reflects a net local share cost of \$235,059,137. This is approximately \$31 million more than the actual local share costs for the twelve months ended September 30, 2003 as presented in the following schedule:

<u>Comparison of Social Services Local Share Costs</u>			
	Tentative	12 Months Ended	Increase
<u>Function</u>	<u>2004 Budget</u>	<u>September 2003</u>	<u>(Decrease)</u>
Administration	\$ 28,624,830	\$ 20,976,841	\$ 7,647,989
MMIS	175,331,796	156,629,120	18,702,676
Medical Asst.	(8,035,475)	(8,888,541)	853,066
Family Asst./TANF	18,709,290	18,757,349	(48,059)
Child Welfare Svc.	13,707,868	13,590,777	117,091
Safety Net	12,433,955	11,072,805	1,361,150
Other Programs	<u>(5,713,127)</u>	<u>(8,028,614)</u>	<u>2,315,487</u>
Total Local Share	<u>\$235,059,137</u>	<u>\$204,109,737</u>	<u>\$30,949,400</u>

Actual 2004 DSS expenditure and revenue transactions must be monitored closely in order to assure any significant budget variances that may occur will be detected in a timely manner.

V. SALE OF TAX LIENS

Several resolutions were adopted by the Erie County Legislature in 2003 that authorized the Commissioner of Finance (Budget Director) to sell County-owned tax certificates representing delinquent real property taxes (March 20, 2003-Comm. 5E-12; June 19, 2003-Comm. 11E-13; and October 2, 2003-Comm. 16E-5 as amended).

The first actual sale of tax certificates occurred on November 6, 2003. The 2004 Tentative Budget reflects a continuation of the County's policy of selling tax certificates and includes revenue of \$15,495,000 for this purpose. Due to the uniqueness of this transaction the Comptroller's Office will be monitoring this account closely.

VI. CAPITAL BUDGET

The 2004 Tentative Capital Budget totals \$63,021,040. To put the 2004 amount in historical perspective, Exhibit F has been included which recaps pertinent information from the adopted capital budgets for 1999 to 2003, as well as the 2004 Tentative Budget.

Regarding the information presented in Exhibit F, the following is significant:

- The amount of bonding needed to provide project financing has risen primarily as a result of the overall increase in the annual capital budgets in recent years.
- The 2004 Tentative Capital Budget does not reflect \$11.6 million of tobacco proceeds that is being provided to the ECMC Healthcare Network.
- The decreased use of tobacco proceeds as a financing source for capital projects from the \$35 million identified in 2001 is mainly attributable to the use of over \$20.7 million, \$21.3 million and \$17.8 million to pay debt service in 2002, 2003 and 2004, respectively.
- The 2001 to 2004 Capital Budgets are substantially larger than those budgets for earlier years. Capital borrowings during the previous Administration were generally capped at \$20 million per year, a cap that is viewed by some as being responsible for producing a considerable backlog of capital projects. The current Administration has substantially expanded the annual capital program and has been greatly assisted in this regard by favorable interest rates and tobacco securitization proceeds. In reality, the budgets from 2001–2004 are even greater than they appear because of presentation changes as compared to the 2000 Capital Budget. Specifically, the 2001 and 2002 budgets are understated by approximately \$22.8 million and \$32.5 million respectively, due to the following: only the estimated five percent local share of the federal road and bridge projects has been included (rather than 100% as in 2000); a project funded with CHIPS monies is now accounted for in the Road Fund; and the use of monies from the Crossroads Arena Reserve project is not budgeted. The 2003 Capital Budget is understated by approximately \$69.8 million (\$32.6 million is for the same reasons cited for the understatements of the 2001 and 2002 budgets, and \$37.2 million is due to the fact that the cost of the capital program as shown in the Tentative Budget was not grossed up to reflect federal, state and local aid that will finance significant portions of various projects administrated by Environment and Planning). The 2004 Capital Budget is understated by approximately \$21.3 million (\$9.7 million is for the same reasons cited for the 2001 and 2002 budget understatements, and \$11.6 million is due to the fact that monies being provided for capital purposes to the ECMC Healthcare Network from tobacco proceeds are included as part of the overall General Fund payments to ECMC).

Also included in Exhibit F is relevant summary data showing that for the 2000 to 2003 Capital Budgets there were significant project approvals/increases outside the annual budget adoption process (\$22.8 million for 2000; \$25.3 million for 2001; \$57.4 million for 2002; and \$22.6 million to date for 2003). The large increase for the 2002 Capital Budget after it was originally adopted compared to the other years is mainly attributable to the approval of \$25 million for the Central Police Training Facility project and \$12 million for the Enterprise Resource Planning

(ERP) project.

Exhibit G compares information for the 1999 to 2004 Capital Budgets primarily based on various categories used in the budget document. The budgetary increases since 1999 relate to five main areas: the Courthouse project; road and bridge projects; Library projects; Parks projects; and those projects classified as general in nature.

Overall, the tentative 2004 Capital Budget continues a trend begun in 2001 of significant increases in the dollar amounts committed for capital purposes, even after considering that some growth would likely occur due to the availability of proceeds from the County's tobacco asset securitization. The proposed financing of capital projects through the issuance of bonds has increased from \$25.4 million for projects approved in the 1999 adopted budget to \$69 million, \$64 million, and \$56.8 million in the two previous Adopted Budgets and the 2004 Tentative Budget, respectively.

The table below provides relevant summary information for the County's outstanding bonds at the end of the years 2000 to 2003:

<u>Project Type</u>	<u>12/31/00</u>	<u>12/31/01</u>	<u>12/31/02</u>	<u>12/31/03</u>
General	\$ 172,781,649	\$ 187,621,420	\$ 229,566,146	\$ 289,746,296
ECMC	35,055,093	27,639,952	21,858,832	15,980,084
Home	<u>7,054,040</u>	<u>5,947,767</u>	<u>4,870,599</u>	<u>4,466,717</u>
Net Debt	214,890,782	221,209,139	256,295,577	310,193,097
Sewer	<u>38,784,478</u>	<u>43,062,717</u>	<u>43,542,940</u>	<u>46,153,108</u>
Total Debt	<u>\$ 253,675,260</u>	<u>\$ 264,271,856</u>	<u>\$ 299,838,517</u>	<u>\$ 356,346,205</u>

The increased capital budgets and the degree of reliance on bonds as a financing source impacts the County's outstanding net indebtedness, which is expected to increase from \$211 million at December 31, 1999 to an estimated \$337 million at the end of 2004, assuming a bond sale of \$50 million next year. It is important to note, however, that even at \$337 million the County will still have only used approximately 15 percent of its debt contracting power.

ECMC

The 2004 Tentative Budget reflects the culmination of an effort initiated some time ago to provide the Erie County Medical Center Healthcare Network with more flexibility to operate. A significant change in the governance structure is now in place to allow the operation of the entity by a public benefit corporation, and it is hoped that the opportunities that it affords will have a favorable significant impact on the hospital's financial condition. The Administration is to be commended for the foresight demonstrated in pursuing this strategy.

In anticipation of ECMC's operation as an independent entity, no budgetary information for it or the Erie County Home was included in the 2004 Tentative Budget. However, given the likelihood that the separation will not occur on January 1, the lack of inclusion of line item budgetary information is inconsistent with the requirements of the County's Administrative

Code. Administration representatives have advised us that a separate line item budget for ECMC is to be filed with the Erie County Legislature as a supplement to the 2004 Tentative Budget by November 10, 2003. The existing budget document does, however, provide \$29.5 million from tobacco monies and the General Fund to ECMC for support throughout the year. This \$29.5 million is made up of \$3.9 million for debt service, \$11.6 million for capital projects, and \$14.0 million for other operational support (including \$1.43 million for School 84).

CONCLUSION

The single most striking aspect of the 2004 Tentative Budget is that it anticipates the retirement of hundreds of employees. While the General Fund budget is mathematically balanced, it needs to be understood that there must be \$17,248,329 in salary cost savings, i.e., money that will not be paid out in 2004 because current employees will opt to retire. This retirement savings is in addition to \$10,615,268 included in the traditionally budgeted payroll turnover account (negative appropriations) in anticipation of positions being vacant during the year for various reasons. Exhibit D illustrates the significant numbers of employees that must retire in order for the County's budget to remain in balance. It is our understanding that at the present time, hundreds of employees have expressed an interest in receiving information regarding retirement, although none has formally committed to retire.

I am available to address any questions or concerns you may have.

Very truly yours,

NANCY A. NAPLES
County Comptroller

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Attachments